No. 88-1400

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1988

FRANCHISE TAX BOARD OF THE STATE OF CALIFORNIA; LEONARD WILSON, Individually and as District Manager, Chicago Office of the Franchise Tax Board of the State of California; and B.M. RARANG, Individually and as Auditor, Chicago Office of the Franchise Tax Board of the State of California,

Petitioners,

vs.

ALCAN ALUMINIUM LIMITED AND IMPERIAL CHEMICAL INDUSTRIES PLC,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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QUESTIONS PRESENTED

1. Whether a foreign company which is the sole stockholder of an American subsidiary has standing to challenge in federal court the accounting method by which the State of California determines the locally taxable income of that subsidiary;

2. Whether, assuming that requisite standing exists in such an instance, a federal action for injunctive and declaratory relief is nevertheless barred by the Tax Injunction Act (28 U.S.C. § 1341) or the principle of comity which underlies the Act.

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Petitioners Franchise Tax Board of the State of California, et al., respectfully pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Seventh Circuit, entered on October 19, 1988.

OPINIONS BELOW

The decision of the United States Court of Appeals for the Seventh Circuit is reported at 860 F.2d 688, and is reprinted in the Appendix at pages A1-A20. The unpublished Memorandum Opinion of the United States District Court for the Northern District of Illinois, Eastern Division, is reprinted in the Appendix at pages A21-A27.

JURISDICTION

The judgment of the Court of Appeals for the Seventh Circuit was entered on October 19, 1988. A timely petition for rehearing, with suggestion that rehearing be held en banc, was denied on January 9, 1989. On January 24, 1989, the Court of Appeals granted petitioners' motion for a stay of the issuance of the mandate for a period of 30 days to enable petitioners to file the present petition. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

28 U.S.C. § 1341:

"The district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State."

STATEMENT OF THE CASE

The consolidated actions that are the subject of this petition were brought by two foreign corporations seeking to challenge, by way of declaratory and injunctive relief, the unitary business/formula apportionment method of accounting under which the Franchise Tax Board of the State of California has proposed to determine the taxable income of the foreign companies' American subsidiaries properly allocable to California.[1] The two suits

were filed in the Northern District of Illinois, with jurisdiction over the subject matter being based on 28 U.S.C. §§ 1331, 1337, 1343 and 2201. Named defendants in one suit are the Franchise Tax Board and two employees assigned to its Chicago office; in the other, the Franchise Tax Board and a single Chicago employee. Said party-defendants are hereinafter collectively referred to as "the Board."

Plaintiffs-respondents, both of which claim that California's method of taxation violates the Foreign Commerce Clause, are Alcan Aluminium Ltd. ("Alcan") and Imperial Chemical Industries PLC ("Imperial"). Alcan, a Canadian company, is the indirect parent of Alcan Aluminum Corporation ("Alcancorp"), a company organized under the laws of Ohio. Imperial, a British company, is the indirect parent of ICI Americas, Inc. ("Americas"), a company organized under the laws of Delaware. Although Alcancorp and Americas are the corporate taxpayers involved here, neither is a party to either lawsuit.

During the years in question, the two American subsidiaries, Alcancorp and Americas, conducted business in California and were therefore subject to the state's corporate tax laws. The Board has determined, or is in the process of determining, the tax liability of these companies under the unitary business/formula apportionment method of accounting. Neither respondent has contested the Board's findings that their respective subsidiaries were engaged in unitary enterprises with their parent companies and other subsidiaries of the parents. Alcan Stip., "Issues," at 2; Imperial Stip., ¶ 30a.[2] Both contend, however, that California's method of taxation imposes an unconstitutional burden on the conduct of their (the parents') foreign commerce. In particular,

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[1] In *Container Corp. v. Franchise Tax Board*, 463 U.S. 159 (1983), this Court upheld the constitutionality of California's method of taxation as applied to a domestic company with foreign subsidiaries, rejecting the contention that California was required to determine the locally taxable income of that company under the separate accounting/arm's length method of taxation used by the Federal Government and various foreign jurisdictions. However, the Court specifically left open the question whether the unitary business/formula apportionment method of accounting is constitutionally permissible when the taxpayer is a domestic subsidiary of a foreign parent. See 463 U.S., at 189, n. 26. The basic distinction between the unitary business/formula apportionment method of accounting and separate geographical accounting is discussed in the *Container* opinion at pages 164-165.

[2] Stipulations of fact, with voluminous exhibits attached, were filed in the District Court in anticipation of the legal issues in the two cases being resolved through cross-motions for summary judgment. Thus, there is a comprehensive factual record in both cases, in contrast to the typical situation in which a court is called upon to decide a question of standing solely or largely on the pleadings.

both have urged that the combined apportionment method of accounting utilized by California results in double taxation of their income and requires that they assume costly compliance burdens.[3]

The audits with respect to Alcancorp that are either completed or underway cover the years 1965 through 1974 and 1976 through 1981. For the years through 1978, the Board has calculated Alcancorp's tax liability on an apportioned share of the total business income of the unitary enterprise of which it is a part. Alcancorp has paid the taxes so calculated for the years 1965 through 1974 and has pursued its administrative remedies with the Board. Alcan Stip., ¶ 36. It has also filed two actions for refund of these taxes in the California courts. *Ibid.*; Exhs. XIX-1 and 2. These actions are still pending. *Ibid.*

The Board has also recomputed Americas' net income subject to California tax for income years ending 1972 through 1981, using as the apportionment base the worldwide income of the unitary enterprise headed by Imperial. Imperial Stip., ¶¶ 10, 14. Americas has paid the resulting assessments for 1972-1975, and has timely filed claims for refund with the Board. Imperial Stip., ¶ 29. The company has also filed a protest of the proposed assessment, calculated on the same basis, for years 1976 through 1981. *Ibid.*

During the audit process, the Board has not directed any correspondence to Alcan or Imperial or to any other group companies not doing business in California. Alcan Stip., ¶ 52; Imperial Stip., ¶ 27. All taxes assessed or proposed to be assessed

[3] The claim of double taxation is based on the fact that the income of the foreign parents and their foreign subsidiaries is included in the preapportioned tax base. Addressing a similar claim, this Court recently stated: "But income that is included in the preapportionment tax base is not, by virtue of that inclusion, taxed by the State. . . . As our Commerce Clause analysis of apportionment formulas has made clear, the inclusion of income in the preapportionment tax base of a state apportionment formula does not amount to extraterritorial taxation." *Shell Oil Company v. Iowa Dept. of Revenue*, ____ U.S. ____, 109 S.Ct. 278, 284, 102 L.Ed.2d 186, 199 (1988).

by the Board are against Alcancorp and Americas. *Ibid.* The Board has not assessed or proposed to assess taxes against either Alcan or Imperial. *Ibid.*

Upon institution of the lawsuits by Alcan and Imperial, the Board filed motions to dismiss, asserting, inter alia, that the respective plaintiffs lacked standing to challenge the state tax treatment of their domestic subsidiaries. The District Court initially ruled in plaintiffs' favor on the standing question. Thereafter, each of the parties moved for summary judgment, with the Board again urging that requisite standing was lacking. On reconsideration of the standing question, the District Court held that respondents were subject to the general rule prohibiting shareholder suits to redress corporate injuries. More specifically, the District Court rejected respondents' claims that they suffer injuries distinct from those of their subsidiaries because California's method of taxation allegedly results in double taxation of their income and requires that they bear a substantial portion of the compliance costs. The District Court accordingly ordered the dismissal of both actions. App., at A27.

Respondents appealed to the Seventh Circuit Court of Appeals, which reversed the order of dismissal and remanded the matter for further proceedings. The Court of Appeals first stated that cases applying the shareholder standing rule fall into two categories: (1) those which bar standing to avoid the manipulation of diversity jurisdiction or a threatened interference with corporate management, and hence "are animated by concerns about the limits on judicial power and the appropriateness of a particular plaintiff bringing a particular action," and (2) those which bar standing to avoid a multiplicity of suits, and hence are animated by the mere "housekeeping concerns" of the federal judiciary. App., at A10-A11. The Court then concluded that a denial of standing in the present cases would serve only the latter objectives, and, implicitly, that standing requirements are less stringent in this category of cases. See, e.g., App., at A11 (". . . in addressing whether injuries to foreign parents are sufficiently direct to confer standing, we attend to which of the several aims of the shareholder standing 'rule' would be served by its invocation"). While apparently agreeing with the District Court that the alleged

compliance costs and double taxation of income would not constitute direct injuries to the parent companies, see App., at A13-A14, the Court went on to find a "direct and independent injury" that had escaped even the attention of respondents. The Court of Appeals held that from the standpoint of foreign companies the unitary business/formula apportionment method of accounting employed by California diminishes the attractiveness of owning American subsidiaries as compared to conducting foreign commerce through contracts with independent companies; that the accounting method therefore burdens foreign companies' decisions to conduct foreign commerce through American subsidiaries; and that this burden on the decision-making of foreign companies is a direct and independent injury sufficient for standing purposes. App., at A15-A17.

Turning next to the proscriptions of the Tax Injunction Act (28 U.S.C. § 1341), the Court of Appeals deemed the Act to be inapplicable to the suits filed by Alcan and Imperial for declaratory and injunctive relief, stating that "the Act has not been construed so broadly as to bar a nontaxpayer (like the parent companies involved here) who lacks a remedy in state court from bringing suit in federal court on the ground that an affiliated taxpayer possesses adequate state court remedies." App., at A18. The Court then considered the principle of comity underlying the Act. It stated that the Act "left intact federal courts' 'discretionary power to grant or withhold relief so as to avoid needless obstruction of the domestic policy of the states,'" and that, in some circumstances, "this discretion, guided by considerations of comity and federalism, may be exercised to bar suits against state tax assessments to which the Tax Injunction Act is inapplicable." App., at A18. It held, however, that "comity and federalism, weighty as these concerns are where the federal courts pass on the constitutionality of state tax legislation, cannot justify withholding federal jurisdiction from a party with no cause of action in state court to redress its own direct and independent injury." App., at A19.

REASONS FOR GRANTING THE WRIT

I

THE COURT OF APPEALS' DECISION ON THE STANDING ISSUE CONFLICTS WITH DECISIONS IN TWO OTHER CIRCUITS

The question whether a foreign company has standing in federal court to challenge the state tax treatment of a domestic subsidiary has been addressed in three previous cases, each of which ruled adversely to the foreign company-stockholder. Two of the decisions were rendered by the Ninth Circuit Court of Appeals: *Shell Petroleum, N.V. v. Graves*, 709 F. 2d 593 (9th Cir. 1983), cert. den., 464 U.S. 1012 (1983), and *EMI Ltd. v. Bennett*, 738 F. 2d 994 (9th Cir. 1984), cert. den., 469 U.S. 1073 (1984). The Court of Appeals in the present matter has virtually conceded that its opinion, which holds that Alcan and Imperial have the requisite standing to pursue such an action, is in conflict with these decisions. See App., at A1 and A17, n. 12.

In addition, however, opposite results were reached in a decision of the District Court of the Southern District of New York that was summarily affirmed by the Second Circuit Court of Appeals: *Alcan Aluminum Ltd. v. Franchise Tax Board*, 558 F. Supp. 624 (S.D.N.Y. 1983), aff'd mem., 742 F. 2d 1430 (2d Cir. 1983), cert. den., 464 U.S. 1041 (1984). While the Second Circuit did not write a full-dress opinion, its summary order affirming the district court opinion stated: "We find appellant's contentions without merit and affirm for substantially the reasons stated in the opinion of the district court reported at 558 F. Supp. 624." The order is reproduced in the Appendix at pages A28-A29.[4]

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[4] The order includes the following footnote: "Since this statement does not constitute a formal opinion of this court and is not uniformly available to all parties, it shall not be reported, cited or otherwise used in unrelated cases before this or any other court." The quotation of the order in the present matter does not fall within that admonition. The order has been available to all parties in the present lawsuits. It was issued in an action brought by Alcan, one of the present plaintiffs, who at that time was represented by Sidley & Austin, a law firm which has

The Foreign Commerce Clause claims in each of the previous cases were substantially identical to the claims advanced by Alcan and Imperial in the present cases. Indeed, as already indicated, one of the previous cases was an unsuccessful attempt by Alcan to obtain the same relief against the Board that it now seeks in the federal court in Illinois.

II

THE COURT OF APPEALS' DECISION CREATES A BASELESS EXCEPTION TO TRADITIONAL STANDING RULES THAT WILL RESULT IN UNPRECEDENTED FEDERAL INTRUSION IN STATE TAX MATTERS

A. Contrary to the decision of the Court of Appeals, the issue of stockholder standing in state tax matters does not implicate mere "housekeeping concerns" of the federal judiciary

This Court has long recognized "the important and sensitive nature of state tax systems and the need for federal court restraint when deciding cases that affect such systems." *Fair Assessment in Real Estate v. McNary*, 454 U.S. 100, 102 (1981). Thus, even prior to the enactment of the Tax Injunction Act (28 U.S.C. § 1341), the Court espoused a principle of equitable restraint in state tax matters. As it explained in *Matthews v. Rodgers*, 284 U.S. 521, 525 (1934):

> "The reason for this guiding principle is of peculiar force in cases where the suit . . . is brought to enjoin the collection of a state tax in courts of a different, though paramount sovereignty. The scrupulous regard for the rightful independence of state governments which should at all times actuate the federal courts, and a proper reluctance to interfere by injunction with their fiscal operations, require that such relief

appeared on behalf of both Alcan and Imperial in this proceeding. Furthermore, the New York case was not "unrelated" to the present matter since Alcan sought in that case to do precisely what it has sought to do here: challenge California's unitary tax treatment of its domestic subsidiary. The Board raised the issue of collateral estoppel before the District Court in Illinois, but that issue was never reached by the court. Consequently, the Board did not address the issue of collateral estoppel in the appeal before the Seventh Circuit.

> should be denied in every case where the asserted federal right may be preserved without it."

The Tax Injunction Act reinforces this principle of noninterference with state tax administration, but does not supplant it. On the contrary, this Court has held that the principle of comity underlying the Act is so compelling as to preclude federal intrusion in state tax matters even in situations not specifically covered by the Act. See *Fair Assessment in Real Estate v. McNary, supra.* (holding that the principle of comity precludes a suit for monetary damages under 42 U.S.C. § 1983); see also *Great Lakes Dredge & Dock Co. v. Huffman*, 319 U.S. 293 (1943).

The Court of Appeals' whole approach to the standing issue in the present matter is inconsistent with this line of authority. When addressing the issue of standing, the Court disregards the fact these stockholder suits seek declaratory and injunctive relief against state taxing authorities. Instead the Court says that since the suits do not involve a manipulation of diversity jurisdiction or a threat to corporate management, the stockholders' standing only implicates the Court's "housekeeping concerns," as opposed to "concerns about the limits on judicial power and the appropriateness of a particular plantiff bringing a particular action." App., at A10-A11. Only *after* the Court concludes that the Board has invoked the stockholder standing rule in an area "where its underpinnings are weakest" (App., at A17), and only *after* the Court concludes that "housekeeping concerns" do not warrant a denial of standing, does the Court proceed to recognize "that 'the principle of comity militates in favor of a stringent standard of justiciability in cases that threaten to interfere with state taxes.'" App., at A19. The Board submits that this is a backward approach to the standing issue which is clearly erroneous. A shareholder's suit brought to challenge state taxation of a corporate taxpayer belongs at the top of the Court of Appeals' totem pole, not at the bottom.

Furthermore, the Court of Appeals' analysis of the stockholder standing rule is historically inaccurate. Even the so-called "traditional limitations on shareholder standing" which the Court places at the top of its totem pole cannot properly be characterized as merely "judge-made restrictions on the availability of the

federal courts." App., at A10. As is evident from this Court's decision in *Hawes v. City of Oakland*, 104 U.S. 450 (1881), a case cited by the Court of Appeals, the rule goes back to the English common law and is based on the fact that a corporation is an entity separate from its stockholders. *Id.*, at 455. The *Hawes* case itself does not represent an application of the stockholder rule as such. Rather, the Court in that case was concerned with the misuse of an *exception* to the stockholder rule, namely, the maintenance in equity of so-called derivative suits. The Court was particularly concerned with increasingly common situations in which corporations, "instead of resorting to the State courts, which are their natural, their lawful, and their appropriate forum" (*id.*, at 452), would collude with an out-of-state stockholder in order to satisfy the requirements of diversity jurisdiction where a federal action was not otherwise available. *Id.*, at 452-453. See also *Daily Income Fund, Inc. v. Fox*, 464 U.S. 523, 529-533 (1983).

The Court of Appeals has missed the parallelism between a collusive suit brought by one of several stockholders to enable a corporation to obtain access to a federal forum, and a suit brought by a sole stockholder of a corporation to accomplish the same objective. Due to the proscriptions of the Tax Injunction Act, neither of the actual taxpayers in the present matter can seek declaratory and injunctive relief against the California tax assessments in federal court. At the same time, though the Court of Appeals is reluctant to concede the point (see App., at A4-A5), it should be evident that the actual taxpayers can voice any and all Foreign Commerce Clause objections to the tax assessments in the state courts. Under these circumstances, the federal suits brought in the names of the sole stockholders serve no purpose other than to provide the corporate taxpayers with a federal forum—a forum to which they would otherwise not be entitled.

B. The Court of Appeals has given no valid basis for concluding that the stockholders involved here suffer direct injuries that are independent of those to the corporate taxpayers

1. The Court's conclusion that the unitary method of taxation burdens the decision-making of foreign companies is based on false premises

The stockholder standing rule cannot be avoided by an allegation of injuries to the stockholder that are the indirect result of wrongs against the corporation. *Pittsburgh & W.Va. Ry. v. U.S.*, 281 U.S. 479, 486-487 (1930). However, as the Court of Appeals has properly recognized, a stockholder may bring an individual action when he is injured directly and independently of the corporation, or, as one court has stated, "where the wrong itself amounts to a breach of duty owed to the stockholder personally." *Schaffer v. Universal Rundle Corporation*, 397 F.2d 893, 896 (5th Cir. 1968).[5]

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[5] The Court of Appeals states in its opinion that "The FTB does not seriously contest plaintiffs' claims that their interest in challenging the California franchise tax satisfies the case or controversy requirement." App., at A5. On the contrary the Board has never accepted the proposition that a shareholder seeking to redress a corporate injury has standing in the constitutional sense. Article III "requires the party who invokes the Court's authority to 'show that he *personally* has suffered some actual or threatened injury . . .'" *Valley Forge College v. Americans United*, 454 U.S. 464, 472 (1982); emphasis added. The legal basis for the general rule that only a corporation and not its shareholders can complain of an injury or wrong done to the corporation is that a stockholder is not personally injured by a wrong done to the corporation; his rights are derivative. *Pittsburgh & Va. Ry. v. U.S.*, 281 U.S. 479, 487 (1930). Thus, although the cases dealing with stockholder standing constitute a line of authority separate from that dealing with standing under Article III, it remains open to question whether a sole or controlling shareholder's ownership interest in a corporation is sufficient by itself (see App., at A5-A6) to satisfy the "injury in fact" requirement of Article III. In any event, even if the "injury in fact" requirement is satisfied, it is clear that such a shareholder may still pursue an individual action only upon the showing of a direct injury which is independent of any injury to the corporation.

In the lower courts, respondents argued that the requirement of a direct and independent injury was satisfied by their allegations that the application of California's unitary method of taxation to their domestic subsidiaries results in double taxation of the parents' income (as well as other income in which the parents have an interest) and requires them to bear substantial compliance costs. As previously noted, the Court of Appeals did not accept this argument. It did, however, discover another "injury" that was not even suggested by respondents: a burden on the foreign companies' decisions to conduct business through American subsidiaries due to the unitary method's potential "to penalize foreign ownership of American assets." App. at 15.[6]

Stated in the form of a syllogism, the Court of Appeals' reasoning appears to be as follows:

MAJOR PREMISE

Foreign companies seeking to sell or purchase products or services in California choose between conducting business through dealings with American subsidiaries or through contracts with unrelated companies.

MINOR PREMISE

When such companies choose to operate through American subsidiaries, and they conduct foreign operations at less cost than in California, a higher proportion of the unitary business' worldwide earnings will be attributed to California than would be the case if the foreign companies engaged in precisely the same foreign commerce through arm's length contracts with unaffiliated companies.[7]

[6] Not only did the respondents fail to raise this argument, but Alcan suggested the reverse: that the unitary method "as applied to foreign parents [sic] has penalized *foreign* activities which increase productivity or develop cheap and abundant resources." Brief of Appellant (Alcan Aluminium Limited), at 36; emphasis added.

[7] This minor premise is drawn from the discussion which appears at pages 16-17 of the Slip Opinion. App., at A15-A16. At page 16, the Court states that, "*These companies* will show a higher taxable income in California under the unitary tax scheme than *they* would [show] if *they* engaged in precisely the same foreign commerce through arm's length contracts with unaffiliated companies." App., at A15. (Emphasis added.) It is therefore evident that the term "[t]hese companies" refers to the foreign parent companies. However, the actual taxpayers in such an instance would be the American subsidiaries operating in California, not their foreign parents. In other words, contrary to what the Court's statement seems to imply, the foreign parents would not "show" *any* "taxable income in California. . . ." Elsewhere (at n. 10) the Court refers to "the proportion of worldwide earnings attributed to California operations." For the sake of accuracy, it is this terminology which has been incorporated in the statement of the minor premise.

CONCLUSION

Therefore, the unitary tax diminishes the attractiveness of owning American subsidiaries in comparison with entering into contracts with independent companies, creating a burden on foreign companies' decisions to conduct business through American subsidiaries.

* * *

The major premise of this syllogism is incomplete insofar as it ignores the fact that foreign companies desiring to conduct business in the United States have a third choice: the conduct of business through branch operations. See, e.g., *Bass, etc., Ltd. v. Tax Comm.*, 266 U.S. 271 (1924) (upholding use of formula apportionment to determine locally taxable income of United Kingdom corporation with branch operations in New York).

The minor premise is so faulty as to destroy the validity of the conclusion. First, the Court of Appeals has erroneously assumed that if a foreign company does business in California through "arm's length contracts with unaffiliated companies," it will have taxable income determinable on a separate accounting basis rather than under the unitary method. Second, the Court has gratuitously assumed (erroneously, the Board believes) that it would be possible for a foreign company to conduct "precisely the

same foreign commerce" through an independent contractor as through an American subsidiary.

With respect to the first assumption, the Court speaks in terms of the unitary method attributing to California "a higher taxable income" or a higher "proportion . . . of worldwide earnings" than would be attributed to California if a foreign company conducted its commerce through unaffiliated companies. Thus, the Court clearly is under the impression that *some* taxable income of the worldwide unitary business, as opposed to a zero amount of income, would be attributed to the state in the latter instance. In fact, whether the parent dealt directly with the unaffiliated company or had its American subsidiary do so, if only the unaffiliated company and not the parent or its subsidiary were doing any business in California, California would attribute *none* of the worldwide unitary business income to California because neither the parent nor the subsidiary would be a taxpayer under California tax law.

If, on the other hand, the activities of a foreign company engaged in a unitary business were such as to give rise to *any* tax liability in California, that liability would be determined by use of unitary formula apportionment regardless of the form in which the foreign company chose to conduct its foreign commerce. If the foreign company operated through an American subsidiary, the taxable income of the subsidiary would be determined under the unitary apportionment method. If the foreign company operated through a branch in California, the taxable income of the foreign company would be determined under the unitary apportionment method. And, finally, if the foreign company operated through an unaffiliated corporation in such a way as to give rise to *any* tax liability on the part of the foreign company, that liability would be determined under the unitary apportionment method, whether or not its relations with the unaffiliated company were deemed to be at "arm's length."[8] Given these circumstances, the

[8] In its reply to the Board's petition for rehearing in the Court of Appeals, Alcan took this to mean that the Board asserts "it can combine for unitary tax purposes two companies that are unaffiliated and are dealing at arms [sic] length." Reply to Petition for Rehearing (Alcan

unitary method cannot be viewed as a burden on the foreign company's decision to conduct foreign commerce in one form or another. The unitary method will be used to determine taxable income attributable to California regardless of the form chosen.

In holding that respondents have requisite standing in this matter, the Court of Appeals has also assumed that foreign companies such as Alcan and Imperial have the option of conducting "precisely the same foreign commerce" through either American subsidiaries or independent contractors. This is difficult to imagine. California has not been a mere market place for the goods produced by the multinational enterprises headed by Alcan and Imperial. The principal activity of Alcan's subsidiary in California during all but one of the 14 years covered by the challenged tax assessments (1965-1978) consisted of the operation of a large manufacturing facility. Alcan Stip., ¶ 6. Similarly, Imperial's subsidiary operates manufacturing and research facilities in California. Imperial Stip., ¶ 8. It is inconceivable that either Alcan or Imperial could conduct "precisely the same foreign commerce" through unaffiliated companies.

Once again, therefore, it is unrealistic for the Court of Appeals to conclude that California's use of the unitary method of taxation in the present case "diminishes the attractiveness of owning American subsidiaries in comparison with entering into contracts with independent companies as a means of engaging in foreign commerce." App., at A15. Such a comparative situation does not exist here. In order to participate in the American economy to the extent they do, Alcan and Imperial must operate either through

Aluminium Limited), at 1-2. That, of course, is incorrect. The point is simply this: If a foreign company engaged in a unitary enterprise were doing business in California through an unaffiliated company in such a manner as to give rise to *any* tax liability on the part of the foreign company, the unitary character of the business would require that the foreign company's tax liability be determined on a formula apportionment basis. This would entail a combined report of only the operations carried on by the *unitary* enterprise within and without the state, not a combined report of the unitary operations and the independent operations of the unaffiliated company.

American subsidiaries or branch operations.[9] What they insist, however, is that the income attributed to the California activities should be determined under the separate accounting/arm's length method of taxation. They have pitted this accounting method against the unitary method, not the use of American subsidiaries against the use of independent contractors.

2. Even if the foreign parents were faced with the choice envisioned by the Court, such a "burden" on their decision-making would not constitute a cognizable injury for standing purposes

As indicated above, the Court of Appeals has apparently assumed that if a foreign company which is part of a unitary business were to engage in commerce in California through contracts with an unaffiliated company, at least some of the income of the unitary business would be attributed to California. Thus, the Court has not gone so far as to suggest that since a foreign company might be able to devise a way to conduct its foreign commerce through an unaffiliated company totally free of California taxes, the imposition of *any* tax against its American subsidiary is such a burden on a foreign company's decision-making as to constitute a sufficient cognizable "injury" to give that foreign company standing to challenge *any* California tax in the federal courts. It has stopped just short of that, however.

The Court of Appeals has held, in effect, that, everything else being equal, a foreign company should not be forced by state tax considerations to select one form of doing business over another. In other words, its underlying thesis seems to be that the potential tax liability arising from the conduct of foreign commerce should be the same, regardless of the form in which the commerce is conducted. It is a fact of life, however, that tax consequences often vary, depending upon the form of doing business, the form of a particular business transaction, etc.

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[9] This was explicitly recognized by Imperial in its opening brief in the Court of Appeals, in which it stated: "Without the existence of Americas, Imperial's considerable commerce with the United States could not exist." Brief of Plaintiff-Appellant Imperial Chemical Industries PLC, at 21.

It is difficult to understand how the resulting "burden" on a company's decision-making can be regarded as a cognizable injury. In the present case, for example, how are the parent companies truly injured if, as assumed by the Court of Appeals, they can conduct "precisely the same foreign commerce" through either American subsidiaries or independent contractors? They are entirely free to select the alternative which, in their view, will have the most favorable tax consequences. Under the reasoning of the Court of Appeals, however, parent companies are injured by having to select between alternatives when they would *prefer* to do business in the form which is the least favorable taxwise. In other words, carried to its logical extreme, the Court of Appeals' decision would permit a foreign company to attack any state tax that negatively impacts on its own preferences.

3. The purported injury to the parent companies is neither "direct" nor "independent" of their status as corporate stockholders

Prudential considerations in general and the shareholder standing rule in particular ordinarily prohibit a party from litigating the legal rights of another. See, e.g., *Allen v. Wright*, 468 U.S. 737, 751 (1984). The legal right at issue in the present matter is the right of the corporate taxpayers to have their tax liability determined in a lawful manner—i.e., in a manner which does not violate the Foreign Commerce Clause. Whether the constitutional issue is litigated in suits for refund brought by the corporate taxpayers in the state courts, or whether their foreign parents are permitted to litigate the issue in federal court, the issue remains the same: Do the taxes assessed against the corporate taxpayers interfere with Congress' power to regulate foreign commerce? Thus, the standing question essentially is whether the parent companies may challenge the constitutionality of tax assessments issued against taxpayer-subsidiaries which are perfectly capable of pursuing the same constitutional claims.

The Court of Appeals has concluded that the foreign parents are injured in such a way as to have standing to litigate their subsidiaries' tax liability. As discussed above, the perceived injury to the parents is tenuous at best. In addition, however, the Court of Appeals has failed to offer any reasoned explanation for

treating the perceived injury to the parent companies as either a "direct" injury or as an injury "independent" of their stockholder status.

If the tax liability of a corporate taxpayer is determined in a manner which violates the Foreign Commerce Clause, it seems self-evident that the party *directly* injured by such a tax determination is the corporate taxpayer against which the unlawful taxes are assessed. Conversely, any injuries to a parent-stockholder in such an instance are necessarily *indirect* since they result from the allegedly unlawful taxes assessed against the corporate taxpayer. The Court of Appeals has not explained its logic for concluding otherwise.

The Court does offer some explanation for treating the perceived injury as one not affecting the foreign companies only in their capacity as stockholders, but its explanation is hardly satisfactory. The Court says that the foreign parents not only own the subsidiaries; they own them "as instrumentalities of the foreign commerce of their parents." App., at A15. But why is this a fact of magical proportions? Every wholly-owned subsidiary can be viewed as an instrumentality by which the parent conducts one type of commerce or another—intrastate, interstate or foreign. The fact that a foreign company utilizes an American subsidiary as an instrumentality of foreign commerce should not, therefore, be considered as creating some sort of special relationship between the two for standing purposes.

The decision of the Court of Appeals to the contrary raises, of course, still other questions. How far does its reasoning go? Is federal standing to litigate state tax matters to be accorded only to foreign companies which own American subsidiaries? If so, what is the justification for the different treatment of domestic companies which utilize various subsidiaries as "instrumentalities" of interstate commerce? If federal standing is not to be so limited, will the federal courts be deluged with suits filed by domestic companies which are dissatisfied with the state tax treatment of their subsidiaries? Meanwhile, what happens to the spirit, if not the letter, of the Tax Injunction Act?

C. The Court of Appeals has confused the issue of respondents' standing with one of the constitutional claims they seek to litigate

A principal contention of respondents on the merits of the controversy is that, when applied to domestic corporations with foreign parents, California's unitary method of taxation violates the "one voice" standard set forth in *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434 (1978). In particular, they have pointed to foreign objections to this method of taxation and to the possibility of foreign retaliation. The Court of Appeals has confused these constitutional claims with the essential question of standing: whether the parent-stockholders, or the corporate taxpayers, are the proper parties to litigate the constitutional claims.

The Court of Appeals states, for example, that "To the extent that California's franchise tax burdens foreign companies' decisions to conduct business through subsidiaries operating in California, it threatens to offend this country's trading partners. . . ." App., at A16. It also states that "It is important that these injuries [to Alcan and Imperial] . . . have fueled a simmering trade controversy which has raised concerns about foreign retaliation and the country's ability to speak with one voice on matters of foreign commerce. . . ." *Id.*, at A17. And at footnote 10 of its opinion, the Court reasons that the unitary method "implicates . . . concerns about foreign retaliation" because it "has the potential to shift a higher proportion of the corporate tax burden onto companies that are affiliated with foreign operations.[10] It continues:

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[10] This potential also exists, of course, in the case of a multinational enterprise headed by a domestic company. It is also unclear what the Court of Appeals means by its statement that, "The potential for the unitary tax to penalize foreign ownership of American assets distinguishes the unitary tax from environmental or safety regulations that might cause comparable increases in the cost of doing business in California, but would presumably affect foreign and domestically owned operations fairly equally." App., at A15. California's tax treatment of foreign and domestically owned operations is the same. Furthermore, assuming arguendo that a foreign company could reduce the cost of doing business in California by choosing to operate solely through independent contractors, thus eliminating the use of foreign factors in

"Evaluation of the constitutional significance of this threat in the particular circumstances presented by California's unitary tax must await the district court's assessment of the merits of this appeal. *We decide only that the potential for constitutionally significant offense is sufficient to create standing.*" (Emphasis added.)

The Court of Appeals has held, in short, that since there may be some merit to the Foreign Commerce Clause claims made by Alcan and Imperial, they have the standing to litigate those claims. This strange twist in standing doctrine puts the cart before the horse. As this Court has repeatedly observed, "standing in no way depends on the merits of the plaintiff's contention that particular conduct is illegal. . . ." *Warth v. Seldin*, 422 U.S. 490, 500 (1975); see also *Flast v. Cohen*, 392 U.S. 83, 99 (1968); *Simon v. Eastern Ky. Welfare Rights Organization*, 426 U.S. 26, 37-38 (1976); *Valley Forge College v. Americans United*, 454 U.S. 464, 476 (1982).

III

THE COURT OF APPEALS' DECISION INVITES WHOLESALE AVOIDANCE OF THE TAX INJUNCTION ACT AND ITS UNDERLYING PRINCIPLE OF COMITY

The historic rule that the federal courts will not interfere with the fiscal operations of the states is codified in 28 U.S.C. § 1341 (the Tax Injunction Act). Section 1341 provides:

"The district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State."

It is well established that 28 U.S.C. § 1341 is an explicit Congressional limitation on the jurisdiction of the federal courts

California's tax computations, exactly the same choice (or in the Court's analysis, exactly the same burden) would be available to domestic parents engaged in foreign commerce by means of a worldwide unitary business.

in the area of state taxation. As this Court stated in *Rosewell v. LaSalle National Bank*, 450 U.S. 503, 522 (1981):

"The statute 'has its roots in equity practice, in principles of federalism, and in recognition of the imperative need of a State to administer its own fiscal operations." *Tully v. Griffin, Inc.*, 429 U.S. (68), at 73. This last consideration was the principal motivating force behind the Act; this legislation was first and foremost a vehicle to limit drastically federal district court jurisdiction to interfere with so important a local concern as the collection of taxes."

Thus, the Act generally prohibits federal courts from granting injunctive relief in cases involving state tax administration; such relief is permitted only in exceptional circumstances where the state court remedy is not "plain, speedy and efficient." *Id.*, at 512. The same rule is applied to requests for declaratory relief. *California v. Grace Brethren Church*, 457 U.S. 393, 408 (1982).

The Court of Appeals in the present matter concluded that the Tax Injunction Act is inapplicable to the actions brought by Alcan and Imperial because "the Act has not been construed so broadly as to bar a nontaxpayer . . . who lacks a remedy in state court from bringing suit in federal court on the ground that an affiliated taxpayer possesses adequate state court remedies." App., at A18. It also concluded that Alcan and Imperial, "which have no standing in state court, cannot be barred from federal court on the strength of the principles of comity and federalism that have sometimes justified abstention from disputes about state taxes pending before state tribunals." App., at A20.

It is true, as the Court of Appeals has observed (App., at A18), that a tax assessment cannot be challenged in the California courts by a party who is not the taxpayer.[11] It makes little sense to

[11] This should come as no surprise. However, the Court of Appeals appears to question the fairness of such a rule, suggesting that California could avoid the disruptive effect of "unwanted federal intrusion" in its tax matters by affording a state remedy to the stockholders of a corporate taxpayer. App., at A19-A20. The theoretical justification for providing such a remedy, apart from the coercive effect of "unwanted

conclude, however, that Alcan and Imperial are thus deprived of effective state remedies. The two wholly-owned subsidiaries (which are more than "affiliated" taxpayers) unquestionably have adequate remedies in the state courts. See, e.g., *California v. Grace Brethren Church, supra,* at 415. And Alcan and Imperial, which have absolute control over their subsidiaries, obviously are in a position to ensure that these remedies are pursued with vigor. In other words, as the sole stockholders of their respective subsidiaries, both of the parent companies effectively *have* state remedies to pursue. Neither was required to bring these lawsuits to ensure a full challenge to the California taxing procedures.[12]

Under these circumstances, it seems entirely reasonable to view the actions brought by Alcan and Imperial as falling within the literal wording of the Tax Injunction Act. The Act does not use the term "taxpayer;" it prohibits injunctive and declaratory relief against state tax assessments "where a plain, speedy and efficient remedy may be had in the courts of [the] State." In any event, it is clear that the purposes of the Act are frustrated if it is read as permitting a sole stockholder to challenge a state tax assessment in federal court when the corporate taxpayer directly concerned is barred from doing so. Accordingly, if the literal language of the Act is not sufficient to prohibit the federal relief sought by Alcan and Imperial, their actions should be dismissed on the basis of the principle of comity which underlies the Act. See, e.g., *Fair Assessment in Real Estate v. McNary,* 454 U.S. 100 (1981). The deference heretofore given to the administration of state taxes cannot rest on such a flimsy foundation as to permit federal intrusion in state tax matters simply because a federal action is

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federal intrusion," is unclear. Moreover, the cure suggested by the Court of Appeals would likely be as disruptive as the ailment.

[12] In addition, it is to be observed that the Seventh Circuit has let Alcan and Imperial have their cake and eat it too. While the Court bases its determination of standing on the fact that Alcan and Imperial have total control over the way their unitary businesses will be conducted in California, the Court then fails to acknowledge that this same control gives the foreign parents the ability to direct fully how their taxpayer subsidiaries will pursue their California tax remedies.

brought in the name of a sole stockholder rather than the corporate taxpayer.

CONCLUSION

Justice Stewart once stated that he could not "imagine a case, at least outside the First Amendment area, where a person whose own [ ] tax liability was not affected could ever have standing to litigate the tax liability of someone else." *Simon v. Eastern Ky. Welfare Rights Org.,* 426 U.S. 26, 46 (1976) (Stewart, J., concurring). This is precisely what Alcan and Imperial are attempting to do in the present matter. They are not the aggrieved taxpayers; rather they are attempting to litigate California's tax treatment of two domestic subsidiaries. The decision of the Court of Appeals reversing the dismissal of their complaints cannot be reconciled with decisions in two other circuits. The decision cannot be reconciled with a reasoned application of the rule prohibiting stockholder suits to redress corporate injuries. And, finally, the decision cannot be reconciled with the proscriptions of the Tax Injunction Act and its underlying principle of comity. It is therefore respectfully submitted that a writ of certiorari should issue.

DATED: February 21, 1989

Respectfully submitted,

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(Appendices follow)

Appendix A

In the

United States Court of Appeals

For the Seventh Circuit

No. 87-2239

Alcan Aluminium Limited,
Plaintiff-Appellant,

v.

Franchise Tax Board of the State of California, et al.,
Defendants-Appellees.

No. 87-2295

Imperial Chemical Industries PLC,
Plaintiff-Appellant,

v.

Franchise Tax Board of the State of California, et al.;
Defendants-Appellees.

Appeals from the United States District Court for the
Northern District of Illinois, Eastern Division.
Nos. 84 C 6932 & 84 C 8902—Ann C. Williams, Judge.

Argued January 20, 1988—Decided October 19, 1988*

* This opinion has been circulated among all judges of this court in regular active service. No judge favored a rehearing in banc because of the arguable conflict with the decisions of the Ninth Circuit in *EMI Ltd. v. Bennett*, 783 F.2d 994 (9th Cir. 1984) and *Shell Petroleum, N.V. v. Graves*, 709 F.2d 593 (9th Cir. 1983).

Before CUDAHY, FLAUM and RIPPLE, *Circuit Judges.*

CUDAHY, *Circuit Judge.* Alcan Aluminium Limited ("Alcan") and Imperial Chemical Industries PLC ("Imperial"), two foreign corporations with American subsidiaries that do business in California, appeal from the district court's dismissal of their constitutional challenge to California's franchise tax. The district court found that the parent companies were injured only in their capacity as shareholders and therefore lacked standing under the well established rule that shareholders must ordinarily demonstrate a direct and independent injury to bring suit. *Alcan Aluminium Ltd. v. Franchise Tax Bd.*, Nos. 84 C 6932, 84 C 8902, mem. op. at 8-10 (N.D. Ill. July 29, 1987). We find that Alcan and Imperial have incurred injuries that are sufficiently direct and independent of the injuries incurred by their subsidiaries to confer standing. We therefore reverse and remand.

I.

Appellants are foreign corporations with majority interests in domestic companies that conduct business in California. Alcan, a Canadian company, is the sole stockholder of Alcan Aluminum Corporation ("Alcancorp"), an Ohio corporation with operations in California.[1] Imperial, an English holding company, owns over fifty percent of ICI Americas, Inc. ("Americas"), a Delaware corporation that also conducts business in California. California's Franchise Tax Board ("FTB") has assessed, or is in the process of assessing, taxes against both Alcancorp and Americas under California's franchise tax law. *See* Cal. Gov't Code §§ 15700-

[1] When Alcan initiated this action for declaratory judgment in August 1984, Alcancorp was directly owned by Alcan Aluminium of Canada, Ltd., which was in turn owned by Alcan Aluminium Limited. A subsequent corporate reorganization renamed Alcan Aluminium of Canada, Limited; it is now called Alcan Aluminium Limited. The entity that was called Alcan Aluminium Limited is now Alcan Aluminium Holdings Limited. This change has no bearing on the issues and we follow the parties' sensible convention of using the original name (shortened to "Alcan") for the foreign parent.

15703 (West 1980 & Supp. 1988); Cal. Rev. & Tax Code § 26422 (West 1979).[2]

California does not employ conventional geographic or transactional accounting techniques to determine the locally taxable income of California businesses that transact business with affiliated companies outside the state. Instead, California, like a number of other states, employs a unitary tax approach—known in the California Code as the "unitary business/formula apportionment method." FTB first determines the scope of the "unitary business" in which a California corporation participates with affiliated companies and calculates the total earnings of this unitary enterprise. It then computes an allocation fraction for each affected taxpayer. This fraction is an unweighted average of three ratios, the ratios of California payroll to total payroll, California property value to total property value and California sales to total sales. Multiplying a corporation's allocation fraction by the total income of the unitary business in which it participates yields that corporation's taxable income for purposes of the franchise tax. Cal. Rev. & Tax Code §§ 25128-25137 (West 1979). The Supreme Court has repeatedly rejected claims, in cases involving domestic parent companies, that this three-factor method violates the commerce clause or foreign commerce clause by unfairly overstating the income attributable to operations in the taxing state. *See Container Corp. v. Franchise Tax Bd.*, 463 U.S. 159, 180-84 (1983); *Mobil Oil Co. v. Commissioner of Taxes*, 445 U.S. 425, 438-39 (1980); *see also Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 271-75 (1978). However, the Court has expressly left open the issue that appellants now seek standing to raise: whether application of the unitary tax to domestic subsidiaries of foreign corporations violates foreign commerce clause prohibitions on multiple taxation and the impairment of federal uniformity. *See Container Corp.*, 463 U.S. at 189 n.26 & 195 n.32;

[2] The stipulated facts reveal that by the end of 1985, the FTB had computed Americas' taxes under the unitary apportionment method for the years 1972 through 1981, and was completing its audits of Alcancorp's California returns for the years 1965 through 1981. The record does not reveal the current status of Alcancorp's and Americas' state-level challenges.

see also Japan Line, Ltd. v. County of Los Angeles, 441 U.S. 434, 446-51 (1979) (discussing concerns about multiple taxation and the national uniformity that are peculiar to foreign commerce context). These questions have prompted heated diplomatic protest and threats of retaliation by the domiciliary countries of affected foreign corporations.

Alcancorp and Americas, appellants' subsidiaries, are in the midst of contesting the FTB's assessments before California administrative officials and courts. The Tax Injunction Act, 28 U.S.C. § 1341 (1982), prohibits the subsidiaries from obtaining review of the constitutionality of the tax by a federal court until they have exhausted their California appeals.[3] The FTB maintains that the subsidiaries have standing to challenge the franchise tax under the foreign commerce clause in California court and, ultimately, in the United States Supreme Court. Appellants seem to assert, though their position on this point is confused and perhaps inconsistent, that their domestic subsidiaries have no standing to challenge the constitutionality of the franchise tax.[4] In

[3] The Act states that "[t]he district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State." 28 U.S.C. § 1341 (1982).

[4] In its opening brief, Imperial stated that Americas "is not engaged in foreign commerce and cannot raise a claim under the Commerce Clause . . . because it has suffered no injury to its foreign commerce." Brief of Plaintiff-Appellant Imperial Chemical Indus. PLC at 14. The FTB's response contested Imperial's idiosyncratic view that Americas could be uninvolved in foreign commerce while Imperial was engaged in foreign commerce by virtue of transactions with Americas. Brief of Appellees, at 23. Imperial's response, that "Americas' foreign commerce is minimal," that the tax "does not directly affect Americas' foreign trade" and that Imperial suffers "the greater loss" from any diminution in trade caused by the tax, do not salvage its position. Reply Brief of Plaintiff-Appellant Imperial Chemical Indus. PLC at 13-14. Nor does the non sequitur that Alcan threw into the breach: "[any] burdens on foreign commerce, . . . must of necessity be burdens exclusively on Appellant, not its U.S. subsidiary, since those burdens relate exclusively to the inclusion of Appellant and its non-U.S. subsidiary's foreign activities

any event, appellants have not given us any convincing reason to doubt that the California courts will entertain Alcancorp's and Americas' foreign commerce clause arguments; so we must proceed on the (perhaps not wholly clear) assumption that the *subsidiaries* can press these constitutional claims in state court.

This case requires us to revisit an issue identified but left unresolved in *Alcan Aluminium Ltd. v. Department of Revenue*, 724 F.2d 1294 (7th Cir. 1984) ("*Alcan II*"). *Alcan II* dismissed Alcan's challenge to Oregon's unitary tax as unripe for adjudication until such time as Oregon actually determined that Alcancorp owed franchise taxes. Although we stressed that the dismissal on ripeness grounds implied no position "as to whether appellant will have standing to challenge appellees' actions if appellees do assess Alcancorp as part of a unitary business including appellant," we stated in dictum that if Alcan's factual allegations were taken as true neither Alcan's shareholder status nor the Tax Injunction Act's bar on federal district court suits for declaratory or injunctive relief against state taxes would prevent Alcan from obtaining standing once the dispute became ripe. *Id.* at 1299. The case before us places the standing issue, an issue which may have important implications for the growing conflict between the United States and nations where parent corporations affected by unitary taxes are domiciled, squarely before this court.

II.

Standing doctrine imposes two types of restrictions on litigants seeking access to federal courts: "constitutional limitations on federal court jurisdiction and prudential limitations on its exercise." *Warth v. Seldin*, 422 U.S. 490, 498 (1975); *see Gladstone, Realtors v. Village of Bellwood*, 441 U.S. 91, 99-100 (1979). The FTB does not seriously contest plaintiffs' claims that their interest in challenging the California franchise tax satisfies the case or controversy requirement of article III, section 2. The plaintiffs'

into the California tax base." Reply Brief of Appellant Alcan Aluminium Limited at 7. Appellants were no more successful in their attempts to illuminate their one-way theory of foreign commerce at oral argument.

ownership interests in their domestic subsidiaries alone, considered apart from the direct harms they incur as participants in foreign commerce (discussed below), clearly give them "such a personal stake in the outcome of the controversy as to assure that concrete adverseness which sharpens the presentation of issues upon which the Court so largely depends for illumination of difficult constitutional questions." *Baker v. Carr*, 369 U.S. 186, 204 (1962).

The dispute here centers on the more elusive, prudential guidelines that the "Court [has] developed, for its own governance in the cases confessedly within its jurisdiction." *Ashwander v. Tennessee Valley Auth.*, 297 U.S. 288, 346 (1936) (Brandeis, J., concurring). The prudential aspect of the standing inquiry, like the constitutional aspect, derives fundamentally from "concern about the proper—and properly limited—role of the courts in a democratic society." *Warth*, 422 U.S. at 498; *see also Duke Power Co. v. Carolina Envtl. Study Group, Inc.*, 438 U.S. 59, 80 (1978); *Peoples Gas, Light & Coke Co. v. United States Postal Serv.*, 658 F.2d 1182, 1195 (7th Cir. 1981). No single formula has been devised for resolving all standing issues in the manifold contexts in which they arise; nothing in the Supreme Court's recent standing decisions belies the observation, now nearly two decades old, that "[g]eneralizations about standing to sue are largely worthless as such." *Association of Data Processing Serv. Orgs., Inc. v. Camp*, 397 U.S. 150, 151 (1970).

Two large and familiar features of the jumbled standing landscape stand out as useful guideposts for our inquiry in this case. First, it is clear that a plaintiff may only bring suit to vindicate a particularized, personal interest. Generalized grievances do not confer standing, nor do claims to relief resting on "the legal rights or interests of third parties." *Warth*, 422 U.S. at 499; *see Tileston v. Ullman*, 318 U.S. 44 (1943). This principle of judicial self-restraint prevents courts from interfering unnecessarily in "abstract questions of wide public significance" that "other governmental institutions may be more competent to address." *Warth*, 422 U.S. at 500.

Second, it is clear that the courts must look to congressional intent when they seek to place appropriate limits on federal

judicial power. In the context of administrative action challenged as violative of the governing statutory standard, the Supreme Court has held that "at bottom the reviewability question turns on congressional intent, and all indicators helpful in discerning that intent must be weighed." *Clarke v. Securities Indus. Ass'n*, 107 S. Ct. 750, 758 (1987); *see Block v. Community Nutrition Inst.*, 467 U.S. 340, 351 (1984). A corollary, more pertinent here, holds that standing to bring constitutional challenges to state actions may be precluded by an express or implied congressional prohibition. In *California v. Grace Brethren Church*, 457 U.S. 393 (1982), for example, the Supreme Court held the Tax Injunction Act, which expressly prohibits taxpayer suits for injunctive relief in order to prevent federal courts from interfering with the assessment of state taxes, impliedly prohibits suits for declaratory relief as well. *Id.* at 407-11.

This case, as we shall see, also implicates judge-made equitable principles under which federal courts have found disputes over state taxes to be nonjusticiable (though typically under the rubric of abstention rather than lack of standing). These principles are distinct from, though consistent with, the comity concerns that Congress sought to protect through the Tax Injunction Act. *See Fair Assessment in Real Estate Ass'n, Inc. v. McNary*, 454 U.S. 100 (1981). The issue is whether, in the circumstances of this case, the equitable principles that favor deference to states on revenue questions outweigh the countervailing obligaton of the federal courts to provide a forum for a litigant with no effective state remedy.

III.

A.

The FTB's arguments against standing purport to rely on these prudential standing principles. First, the FTB argues that the injuries of which Alcan and Imperial complain are indirect injuries incurred by the appellants in their capacity as shareholders of Alcancorp and Americas. The FTB contends that the prudential bar on standing to enforce third parties' rights encompasses a well established prohibition on shareholder suits to

redress injuries to their corporations. Longstanding equitable restrictions on shareholder suits, the FTB points out, generally prohibit shareholders from initiating actions to enforce the rights of the corporation unless they can demonstrate that they have taken appropriate steps to persuade the corporate managers to pursue the same action and that the managers refused for reasons other than good faith business judgment. *See Twohy v. First Nat'l Bank*, 758 F.2d 1185, 1194 (7th Cir. 1985); *Swanson v. Traer*, 249 F.2d 854, 859-61 (7th Cir. 1957); *see also* Fed. R. Civ. P. 23.1 (requirements for bringing shareholder derivative action in federal court). An exception to this rule exists, however. Shareholders with direct, personal interests in a cause of action can bring suit even if the corporation's legal rights and obligations are also implicated. *Simcox v. San Juan Shipyard, Inc.*, 754 F.2d 430, 438 (1st Cir. 1985); *Buschmann v. Professional Men's Ass'n*, 405 F.2d 659, 661-63 (7th Cir. 1969); *Schaffer v. Universal Rundle Corp.*, 397 F.2d 893, 896 (5th Cir. 1968) (stockholder may bring an individual action "where the wrong itself amounts to a breach of duty owed to the stockholder personally").

This case requires us to determine whether Alcan's and Imperial's particular injuries are sufficiently direct and personal to confer standing. The parent companies contend that they are directly injured because they incur significant accounting costs as a result of California's reliance on a unitary tax base, because California effectively taxes the income of overseas affiliates that is already subject to taxes in other jurisdictions and because the tax impairs their subsidiaries' value as instrumentalities of foreign commerce. The FTB counters that each of the harms described by the appellants was incurred indirectly, through the parent corporations' status as shareholders in Alcancorp and Americas.

To determine the scope of the exception, we must consider the nature and purposes of the shareholder standing rule. Limitations on shareholder derivative suits in federal courts were originally imposed to curb the use of shareholder suits as a means of invoking diversity jurisdiction when the corporation itself could not. *See Hawes v. City of Oakland*, 104 U.S. 450, 459-60 (1881); *see generally* 7C C. Wright, A. Miller & M. Kane, *Federal Practice and Procedure* § 1821 at 10-13 (1986) (describing con-

text of the *Hawes* holding and its subsequent codification in federal rules). Later, the Supreme Court indicated that the bar on shareholder standing also protects the rights of shareholders who control a majority of voting shares to make binding decisions about the enforcement of corporate rights. *See, e.g., Corbus v. Alaska Treadwell Gold Mining Co.*, 187 U.S. 455, 463 (1903) ("It is not a trifling thing for a stockholder to attempt to coerce the directors of a corporation to an act which their judgment does not approve, or to substitute his judgment for theirs."); *see also Swanson*, 249 F.2d at 859-60.[5] Courts and commentators have since recognized that the deterrence of "strike suits," shareholder derivative actions brought for the purpose of eliciting lucrative settlements from management rather than to force the corporation to pursue some viable cause of action, is an important objective underlying the shareholder standing requirements. *See, e.g., Lewis v. Curtis*, 671 F.2d 779, 788 (3d Cir.), *cert. denied*, 459 U.S. 880 (1982); *Brink v. Dalesio*, 667 F.2d 420, 428 (4th Cir. 1981); Note, *Trust Beneficiary Standing in Shareholder Derivative Actions*, 39 Stan. L. Rev. 267, 273-74 (1986).

In a number of more recent cases, federal courts have denied individual standing to shareholders notwithstanding that these shareholders controlled a majority of voting shares and that subject matter jurisdiction did not depend on the individual plaintiff's residence. In *Gregory v. Mitchell*, 634 F.2d 199 (5th Cir. 1981), for example, controlling shareholders in a bank were prevented from suing as individuals under 42 U.S.C. section 1983 for alleged discriminatory treatment by state regulators. *Accord Jones v. Niagara Frontier Trans. Auth.*, 836 F.2d 731, 736 (2d

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[5] Justice Brandeis' concurrence in *Ashwander v. Tennessee Valley Authority*, 297 U.S. 288, 342-44 (1936), relied in part on the rights of shareholder majorities to support his contention that the shareholder plaintiffs lacked standing. Chief Justice Hughes' lead opinion (which, like Justice Brandeis' concurrence, garnered four votes) found standing based on stockholders' allegations that corporate directors' breached a duty to stockholders by failing to oppose illegal government action. *Id.* at 318-23. Both opinions looked to the purposes for limiting shareholder standing and the particular facts of the case at hand to assess the status of the plaintiffs in that case.

Cir. 1987); *Erlich v. Glasner*, 418 F.2d 226 (9th Cir. 1969); *see also, e.g., Sherman v. British Leyland Motors, Ltd.*, 601 F.2d 429, 439-40 (9th Cir. 1979) (sole shareholder in automobile dealership cannot sue in individual capacity in claims arising under Automobile Franchise Act, antitrust laws or in pendent state claims); *Von Brimer v. Whirlpool Corp.*, 536 F.2d 838, 846 (9th Cir. 1976) (majority shareholder barred from suing for interference with corporation's contractual relations; following rule "avoids multitudinous litigation and recognizes the corporate entity"); *Smith v. Martin*, 542 F.2d 688, 690 (6th Cir. 1976), *cert. denied*, 431 U.S. 907 (1977). *But see Leverett v. City of Pinellas Park*, 775 F.2d 1536, 1538-39 (11th Cir. 1985) (liberal approach to standing in first amendment area makes shareholder standing bar inapplicable where individuals seek to raise corporation's first amendment claims). None of these decisions provides a detailed justification for applying the rule against shareholder standing to situations where shareholder suits do not threaten to circumvent the limits on diversity jurisdiction or to undermine managerial decisionmaking. *Von Brimer* and *Erlich*, however, suggest that in this context, the prohibition on shareholder actions rests primarily on considerations of judicial economy and the importance of avoiding a multiplicity of suits. *See Von Brimer*, 536 F.2d at 846; *Erlich*, 418 F.2d at 228. *See generally* 12B W. Fletcher, *Cyclopedia of the Law of Private Corporations* §§ 5909-5911 (rev. perm. ed. 1984).

This brief overview points up an important difference between limitations on shareholder standing and the general prudential requirements. Though prudential in the sense that they are judge-made restrictions on the availability of the federal courts, traditional limitations on shareholder standing derive from broader origins than do the general prudential restrictions. When courts bar shareholders from bringing suit in order to prevent corporations from circumventing statutory limits on diversity jurisdiction or to prevent minority shareholders from interfering with the operation of the corporation, they are animated by concerns about the limits on judicial power and the appropriateness of a particular plaintiff bringing a particular action—issues at the core of what we have been calling the prudential aspect of the standing question. But when courts bar shareholder suits solely to avoid a

multiplicity of suits and to conserve judicial resources, in situations where neither the manipulation of diversity jurisdiction nor the maintenance of majority control is at issue, they are animated by qualitatively different concerns. The focus in this latter class of cases is on "'[w]ise judicial administration, giving regard to conservation of judicial resources and comprehensive disposition of litigation,'" *Colorado River Water Conservation Dist. v. United States*, 424 U.S. 800, 817 (1976) (quoting *Kerotest Mfg. Co. v. C-O-Two Fire Equip. Co.*, 342 U.S. 180, 183 (1952)). In deciding whether to abstain from a controversy in deference to a parallel state court proceeding—a decision resembling the prudential aspect of a standing determination both in its effect and in its attention to prudential considerations—the Supreme Court has held that the conservation of judicial resources can only in "exceptional circumstances" justify the withholding of federal jurisdiction in spite of "the virtually unflagging obligation of the federal courts to exercise the jurisdiction given them." *Id.; see Moses H. Cone Memorial Hosp. v. Mercury Constr. Co.*, 460 U.S. 1, 13-19 (1983).[6] While the courts' housekeeping concerns certainly warrant consideration, we believe that *Colorado River* and *Moses H. Cone* place them on a lower footing than concerns about preventing the courts from trenching on the prerogatives of elected officials. Thus, in addressing whether injuries to foreign parents are sufficiently direct to confer standing, we attend to which of the several aims of the shareholder standing "rule" would be served by its invocation.[7]

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[6] *Colorado River* does list federal court actions to restrain the collection of state taxes as one of the few categories of cases in which abstention may be appropriate. 424 U.S. at 816. We discuss the comity and federalism argument for denying standing in Part II. B. below.

[7] Our research has revealed only two cryptic references to the relationship between shareholder standing rules and the general prudential limits on standing. *See Shell Petroleum, N.V. v. Graves*, 570 F. Supp. 58, 63 n.6 (N.D. Cal.) ("The requirement that a shareholder establish injury to rights specifically vested in it individually, distinct from those of the corporation . . . might or might not be a particular instance of the more general prudential standing principles quoted above. But in any event, the requirement must be satisfied."), *aff'd*, 709 F.2d 593 (9th

Only a handful of decisions have considered whether foreign parents have standing to contest the constitutionality of unitary taxes assessed on their domestic subsidiaries. In general, they have denied standing; and they have all relied upon a broad formulation of the rule limiting shareholder standing. In *Shell Petroleum, N.V. v. Graves*, 709 F.2d 593, 595-56 (9th Cir.), *cert. denied*, 464 U.S. 1012 (1983), the Ninth Circuit found that the injury suffered by a parent corporation due to the multiple taxation of foreign income was indirect, entirely derivative of injuries to its California subsidiary.[8] *Accord EMI Ltd. v. Bennett*, 738 F.2d 994, 996-99 (9th Cir.), *cert. denied*, 469 U.S. 1073 (1984). Similarly, a New York district court has held, and the Second Circuit has affirmed, that Alcan lacked standing to sue the FTB because Alcan had not demonstrated that it incurred a direct injury or that the FTB owed Alcan some independent duty. *Alcan Aluminium Ltd. v. Franchise Tax Bd.*, 558 F. Supp. 624, 628-29 (S.D.N.Y.), *aff'd mem.*, 742 F.2d 1430 (2d Cir. 1983), *cert. denied*, 464 U.S. 1041 (1984) (hereinafter "*Alcan I*").[9] The district court rejected Alcan's claim that the unconstitutional

Cir.), *cert. denied*, 464 U.S. 1012 (1983); Note, *The Demand and Standing Requirements in Stockholder Derivative Actions*, 44 U. Chi. L. Rev. 168, 168 n.5 (1976) ("'Standing' in the context of derivative actions is not to be confused with its more traditional meaning as defining when an individual can challenge governmental action.").

[8] *Shell* also affirmed the district court's alternative holding that Shell's claim would not be ripe until its American subsidiaries had exhausted their remedies before California administrative bodies. 709 F.2d at 596-97. The district court held that even if Shell had not run afoul of the prohibition on shareholder standing, its injury would not be sufficiently certain and immediate to be deemed ripe until its subsidiaries had exhausted their state-level challenges. *Shell Petroleum, N.V.*, 570 F. Supp. at 65-66. The district court predicated this strict ripeness requirement on the comity and federalism concerns that gave rise to the Tax Injunction Act and the Supreme Court's continuing recognition of limits on its equity powers even where the Act is inapplicable. *Id.* at 66. We discuss these matters further below.

[9] An earlier district court decision in *Alcan I* stayed federal court proceedings, including resolution of the standing issue, pending resolution of Alcan's challenges before state administrative bodies and courts.

taxation of an "instrumentality of foreign commerce" in its control constituted a direct injury sufficient to confer standing. *Alcan I*, 558 F. Supp. at 629.

There may well be some merit to the discussions of compliance costs and the double taxation of income in these decisions insofar as these factors, *in themselves*, were deemed insufficient to constitute direct injuries to the parent companies. The information demands of which Alcan and Imperial complain were presented, as the district court pointed out, to Alcancorp and Americas, not to their foreign parents. Mem. op. at 10. Alcan and Imperial may find it in their interest to expend the considerable sums that they say will be required to produce the worldwide figures for the unitary enterprises that California has requested from their subsidiaries. Or they may find it more advantageous to accept the penalties that California will impose on its subsidiaries for failing to produce the figures. In either event, one could view the information demands as affecting Alcan and Imperial by reducing the profitability of their California operations, net of the administrative costs that these operations impose on the world-

Alcan Aluminium Ltd. v. Franchise Tax Bd., 539 F. Supp. 512, 516 (S.D.N.Y. 1982).

Because Alcan lost on standing grounds in *Alcan I*, one might have expected the FTB to pursue a collateral estoppel defense in this action. *See Planned Parenthood Ass'n v. Kempiners*, 700 F.2d 1115, 1138 (7th Cir. 1983). Indeed, the FTB did move to dismiss Alcan's complaint on collateral estoppel grounds in the district court, but its motion was denied. The FTB's cross-motion for summary judgment requested reconsideration of collateral estoppel as an alternative basis for dismissing Alcan's suit, but the district court did not discuss this argument.

On appeal, the FTB virtually ignores this issue. It characterizes *Alcan I* first as "[a]n action similar to the present one," Brief of Appellees at 11 n.5, and later as a case that "alleged grounds for relief . . . substantially identical to those asserted here," *id.* at 29. Appellees' only reference to collateral estoppel appears in a footnote discussing the fate of the collateral estoppel claim in the district court. This is notably less than the presentation of legal authority and facts about the two cases that would be required for us to address the collateral estoppel argument on appeal. *See Bonds v. Coca-Cola Co.*, 806 F.2d 1324 (7th Cir. 1986); *Manbourne Inc. v. Conrad*, 796 F.2d 884, 888, 890 n.6 (7th Cir. 1986).

wide enterprises. By possible analogy if California enacted environmental or worker safety regulations requiring corporate taxpayers to produce costly information obtainable only through their foreign parents, it would be questionable whether foreign parents would have independent standing to challenge those regulations (at least so long as there was no indication that the regulations were not a mere pretext for raising costs of foreign-owned enterprises). Of course, it is entirely possible, though Alcan and Imperial have made no such claim here, that some parent companies' accounting systems attribute some of the costs of complying with unitary tax systems (or with environmental regulations) to foreign affiliates. But the nominal incidence of compliance costs under a company's own accounting system would not, in itself, normally be determinative of "direct" injury. The compliance costs can be viewed, in principle, as an increase in the overhead of the California operations; under that view, the foreign parents incur harm as shareholders in an enterprise faced with increased costs. *See EMI Ltd.*, 738 F.2d at 997; *Shell Petroleum, N.V.*, 709 F.2d at 595-96; *see also Alcan I*, 558 F. Supp. at 628-29 & n.9.

Somewhat similar considerations may apply to the double taxation claim, although only as that claim is narrowly construed. Alcan and Imperial point out that California's unitary tax scheme is inconsistent with the transactional approach employed by most if not all foreign nations (as well as the United States government), which allocates profits among affiliated operations by estimating the distribution of profits that would result from arm's length transactions. Alcan and Imperial contend that California's taxation of corporate income, on which foreign affiliates must pay taxes to their host governments under a transactional tax system, directly injures the foreign parents. But it is possible to view these taxes, like compliance costs, simply as added costs for the domestic subsidiary, experienced by the foreign parent as a decline in the after-tax profits of its California operations. *See EMI Ltd.*, 738 F.2d at 996 (parent's "only real connection to the live controversy is in its status as majority shareholder"); *Shell Petroleum, N.V.*, 709 F.2d at 595 ("[unitary] method of taxation . . . does not injure [parent] directly or independently of the corporation").

However, the arguments that Alcan and Imperial incur no direct and independent injury from costs plausibly viewed as burdens on their subsidiaries remains persuasive only so long as the relationship between parents and subsidiaries is viewed narrowly, focusing exclusively on the parents' status as shareholders. It is indisputable that, but for their ownership of stock in corporations that operate in California, Alcan and Imperial would have no complaint about either compliance costs or double taxation. This line of argument, however, ignores a second important feature of the relationship between the foreign parents and their domestic subsidiaries: the subsidiaries are owned as instrumentalities of the foreign commerce of their parents. Foreign companies seeking to sell or purchase products or services in California choose between conducting business through dealings with American subsidiaries or through contracts with unrelated companies. Plaintiffs allege that for many enterprises subject to the unitary tax, the earnings of operations in California, computed under the arm's length transaction approach, are lower in relation to labor costs, capital assets and sales than are the similarly computed earnings of related operations in countries other than the United States. These companies will show a higher taxable income in California under the unitary tax scheme than they would if they engaged in precisely the same foreign commerce through arm's length contracts with unaffiliated companies. From the perspective of the foreign parent, therefore, the unitary tax diminishes the attractiveness of owning American subsidiaries in comparison with entering into contracts with independent companies as a means of engaging in foreign commerce. The potential for the unitary tax to penalize foreign ownership of American assets distinguishes the unitary tax from environmental or safety regulation that might cause comparable increases in the cost of doing business in California, but would presumably affect foreign and domestically owned operations fairly equally. It is the incidence of the unitary tax, its potential to disfavor a particular mode of foreign participation in the American economy, rather than the

magnitude of the costs it imposes that provides the strongest argument for standing.[10]

Viewed in these terms, Alcan's and Imperial's injuries are direct and independent of the injury to their subsidiaries and standing should follow. To the extent that California's franchise tax burdens foreign companies' decisions to conduct business through subsidiaries operating in California, it threatens to offend this country's trading partners, many of whom must deal with conflicting internal views on the proper role of American investment in their economies, and to elicit retaliatory measures. Concern about precisely this type of foreign response to states' taxation of foreign interests has led the Supreme Court to find stricter limits on state taxes in the foreign commerce clause than in the interstate commerce clause. *Japan Line*, 441 U.S. at 444-45. The record in this case contains numerous indications that foreign governments view California's and other states' sharp departures from the international norm of taxing corporate income based on transactional allocations of income as a source of serious injury to multinationals located within their borders and a

[10] The tax burden on companies subject to California's franchise tax will depend, of course, on the tax rate as well as on the proportion of worldwide earnings attributed to California's operations. A state that applies a high tax rate to earnings computed according to the arm's length transaction method can depress after-tax earnings available to a foreign parent more than a state that applies a lower rate to the unitary revenues. *See Container Corp.*, 463 U.S. at 195. However, a unitary tax system has the potential to shift a higher proportion of the corporate tax burden onto companies that are affiliated with foreign operations. It is this possibility that implicates the concerns about foreign retaliation that have guided the court's interpretation of the foreign commerce clause. *See Japan Line*, 441 U.S. at 456; *see also Container Corp.*, 463 U.S. at 189 n.26, 195 n.32 (noting possibility that application of unitary tax to domestic subsidiaries of foreign companies may offend trading partners); *cf. Asahi Metal Indus. Co. v. Superior Court*, 107 S. Ct. 1027, 1034-35 (1987). Evaluation of the constitutional significance of this threat in the particular circumstances presented by California's unitary tax must await the district court's assessment of the merits of this appeal. We decide only that the potential for constitutionally significant offense is sufficient to create standing.

threat to commercial relations with the United States.[11] To be sure, burdening the use of California subsidiaries as an instrumentality of foreign commerce does not necessarily harm Alcan and Imperial exclusively. Alcancorp and Americas may incur parallel injuries by virtue of their participation in the same foreign commerce. But the choices about the manner in which international trade is to be conducted are primarily the parents' choices. To dismiss the injury to the foreign parents caused by the distortion of these choices as indirect and derivative is to expand the shareholder standing rule in an area where its underpinnings are weakest. While we might save some federal courts' resources by confining foreign parents to their subsidiaries' remedies in state tribunals, to achieve these marginal savings we would have to overlook the real sense in which California's franchise tax directly and independently injures Alcan and Imperial. It is important that these injuries, which the FTB would have us label indirect under an expansive view of the shareholder standing bar, have fueled a simmering trade controversy which has raised concerns about foreign retaliation and the country's ability to speak with one voice on matters of foreign commerce—concerns that are central to the purposes of the foreign commerce clause.[12]

[11] *See, e.g.*, United Kingdom Finance Act of 1985, New Clause 27 (authorizing Treasury of United Kingdom, subject to parliamentary review, to withdraw United Kingdom tax credit from United States companies with substantial operations in unitary tax states), *reprinted in* Appendix to the Brief of Plaintiff-Appellant Imperial Chemical Indus. PLC, Item 8; Brief Amicus Curiae Filed on Behalf of the Member States of the European Communities and the Governments of Australia, Japan and Switzerland, No. 87-2295 at 2 (Aug. 27, 1987) ("This case involves issues of vital importance to the fifteen countries and to their future economic and commercial relations with the U.S.").

[12] Insofar as the Ninth Circuit's decisions in *Shell Petroleum, N.V.* and *EMI Ltd.*, may conflict with our holding, we are not persuaded to follow them.

B.

The FTB also asserts that Alcan and Imperial are barred from federal court by the principles of comity that have traditionally deterred federal courts from interfering with state revenues. These principles were partially codified in the Tax Injunction Act, which prohibits district courts from enjoining, suspending or restraining state taxes "where a plain, speedy and efficient remedy may be had in the courts of such State." 28 U.S.C. § 1341 (1982). But that Act is inapplicable here. The Act has been interpreted broadly, in light of Congress' intent "to prevent federal-court interference with the assessment and collection of state taxes," to bar declaratory as well as injunctive relief for plaintiffs with adequate state remedies. *California v. Grace Brethren Church*, 457 U.S. 393, 411 (1982). The Court has also adopted a lenient construction of the "plain, speedy and efficient" proviso. *Id.* at 412-13; *Rosewell v. LaSalle Nat'l Bank*, 450 U.S. 503, 512-14 (1981). However, the Act has not been construed so broadly as to bar a nontaxpayer (like the parent companies involved here) who lacks a remedy in state court from bringing suit in federal court on the ground that an affiliated taxpayer possesses adequate state court remedies. The FTB concedes that California's administrative and judicial remedies are available only to the taxpaying subsidiaries and not to their parents. Thus, the Tax Injunction Act does not, by its terms, undermine Alcan's and Imperial's entitlement " 'to a judicial remedy in which they can participate as a party.' " *Alcan II*, 724 F.2d at 1297 (quoting *Capitol Indus.-EMI, Inc. v. Bennett*, 681 F.2d 1107, 1119 (9th Cir.), *cert. denied*, 455 U.S. 943 (1982)).

The inapplicability of the Tax Injunction Act, however, does not settle the issue. The Act left intact federal courts' "discretionary power to grant or withhold relief so as to avoid needless obstruction of the domestic policy of the states." *Great Lakes Dredge & Dock Co. v. Huffman*, 319 U.S. 293, 298 (1943). In some circumstances, this discretion, guided by considerations of comity and federalism, may be exercised to bar suits against state tax assessments to which the Tax Injunction Act is inapplicable. *See Fair Assessment in Real Estate Ass'n Inc. v. McNary*, 454 U.S. 100, 110-13 (1981) (suit for money damages under 42

U.S.C. section 1983); *Great Lakes*, 319 U.S. at 298-99 (suit for declaratory judgment);[13] *see also Colorado River*, 424 U.S. at 816 (aversion to interference with state revenues represents one of few, limited grounds for federal abstention); *cf. Burford v. Sun Oil Co.*, 319 U.S. 315, 332-34 (1943) (abstention from request to enjoin order of regulatory commission where suit "involves basic problems of [state] policy"). In *Alcan II*, we held that "the principle of comity militates in favor of a stringent standard of justiciability in cases that threaten to interfere with state taxes." 724 F.2d at 1298. Justiciability in that case turned on a ripeness question: whether the costs to a foreign parent of producing the information required for a unitary tax audit, before the unitary tax in question had even been held applicable, were "sufficient to overcome the prudential considerations of comity." *Id.* at 1299. While we held that the controversy was not yet ripe, we declined to address whether the same prudential concerns would deprive the parent corporation of standing in the event that the audit produced a determination that the unitary tax applied. *Id.*

We hold that comity and federalism, weighty as these concerns are where federal courts pass on the constitutionality of state tax legislation, cannot justify withholding federal jurisdiction from a party with no cause of action in state court to redress its own direct and independent injury. This is especially true where important, and apparently pressing, considerations of international comity as well as comity within our own federal system are at stake. Neither *Great Lakes* nor *McNary*, in which the Supreme Court invoked equitable abstention to avoid federal court interference with state revenue sources, turned aside parties who could not themselves sue in state court.[14] It is also significant that

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[13] *Great Lakes* declined to decide whether the Tax Injunction Act applied to suits for declaratory judgment, reasoning that considerations of comity justified the refusal to hear such a suit even if the statute did not literally apply. Subsequently, *California v. Grace Brethren Church* revisited the issue and expressly held that the Act did not distinguish between suits for declaratory and injunctive relief. 457 U.S. at 408-11.

[14] In *Alcan Aluminium Ltd. v. Franchise Tax Bd.*, 539 F. Supp. 512, 515-16 (S.D.N.Y. 1982), the district court did invoke equitable abstention to stay Alcan's federal suit, despite Alcan's lack of standing in state

California presumably possesses a ready remedy for unwanted federal intrusion. To eliminate federal court jurisdiction over disputes of this nature, the state need only provide foreign parent companies with a "plain, speedy and efficient' remedy of their own in state court. *See Capitol Indust.-EMI*, 681 F.2d at 1119 n.32; *Alcan Aluminium*, 539 F. Supp. at 516 n.9. With such effective means of self-help for the state so near at hand, we cannot conclude that comity requires us to deny plaintiffs the opportunity to appear as named parties to litigate their constitutional claims.

IV.

We find that Alcan and Imperial, owners of controlling interests in American subsidiaries that function as instrumentalities of their foreign commerce, have alleged injuries resulting from California's franchise tax that are sufficiently direct and independent of the injuries to their subsidiaries to confer standing. We further find that the foreign parent companies, which have no standing in state court, cannot be barred from federal court on the strength of the principles of comity and federalism that have sometimes justified abstention from disputes about state taxes pending before state tribunals. We therefore reverse and remand for further proceedings.

REVERSED AND REMANDED

A true Copy:
Teste:

Clerk of the United States Court of Appeals for the Seventh Circuit

court. The stay remained in force for nine months before it was superseded by an order dismissing the suit on standing grounds. *See Alcan I*, 558 F. Supp. 624.

Appendix B

In the United States District Court
for the Northern District of Illinois
Eastern Division

No. 84 C 6932

Alcan Aluminum Limited,
Plaintiff,

v.

Franchise Tax Board of the State of California, et al.,
Defendants.

No. 84 C 8902

Imperial Chemical Industries PLC,
Plaintiff,

v.

Franchise Tax Board of the State of California, et al.,
Defendants.

MEMORANDUM OPINION AND ORDER

In these related cases, the plaintiffs Alcan Aluminum Limited ("Alcan") and Imperial Chemical Industries PLC ("Imperial") are corporations who are based and only do business in countries other than the United States. Alcan and Imperial each wholly own a subsidiary corporation doing business in California. The defendant Franchise Tax Board of the State of California[1] ("Board"), which has the power and duty to administer the California tax laws, has assessed on those subsidiaries an income tax pursuant to California's system of worldwide unitary income taxation. Alcan and Imperial assert that the unitary income tax as applied in this case is an unconstitutional burden on foreign commerce. But because the court finds that neither Alcan nor Imperial have standing to challenge the tax assessments on their

[1] Alcan and Imperial have also named as defendants a number of officers of this organization.

domestic subsidiaries, the court dismisses both cases without reaching the foreign-commerce claims.

Alcan is a corporation organized and existing under the laws of Canada. Its headquarters and principal place of business are in Montreal, Quebec. Alcan and its various subsidiaries are engaged in all phases of the aluminum business on an international scale. Although Alcan itself does not do business in the United States, it indirectly owns all of the issued stock of Alcan Aluminum Corporation ("Alcancorp"), a corporation organized under the laws of Ohio and with its principal place of business in Cleveland. Alcancorp fabricates and sells various aluminum products in the United States. Alcancorp conducts a portion of its business in California.

Imperial is an English public limited company having its principal offices and place of business in London, England. Imperial has about 400 subsidiaries in which it has more than a fifty-percent ownership interest. Imperial itself does not do business in California or elsewhere in the United States, but Imperial's wholly owned subsidiary, ICI Americas Inc. ("Americas"), does do business in California. Specifically, since 1971 Americas has conducted business in California principally through the operation of a pharmaceutical manufacturing plant in Pasadena as well as other sales and manufacturing activities.

The Board is an official California agency whose responsibilities include administration, collection and enforcement of the state's corporate income and franchise taxes. The "unitary apportionment" formula used by the Board is a method of determining the amount of income of a taxpayer attributable to and taxable by California. Under this method, all business activities that are deemed to function as a "unitary" business are combined. The portion of the combined income attributable to activities in California is determined by a formula that compares the property, payroll and sales of the unitary business in California to the property, payroll and sales of the unitary business everywhere.

For the tax years in question, the Board determined that Alcancorp and Americas were part of a worldwide unitary business that included their foreign parent corporations, Alcan and

Imperial respectively. Based upon this determination, the Board computed the subsidiaries' business income subject to the California tax by applying the aforementioned three-factor apportionment formula. The resulting tax liability for each of the subsidiaries was greater than it otherwise would have been had the Board used the most commonly used international accounting principles.

Subsequently, Alcan and Imperial brought these separate suits in which they allege that the unitary apportionment method of accounting is an unconstitutional burden on the United States' ability to regulate foreign commerce. *See* U.S. Const. art. I, § 8, cl. 3. Specifically, the foreign parent corporations request that this court enjoin the Board from assessing, levying or collecting any tax from their domestic subsidiaries based upon the unitary apportionment formula because of the risk of double taxation, the cost of compliance incurred by the foreign parents and the objections of and possible retaliation by foreign governments. On January 1, 1985, Judge Marshall made the finding that these cases were related. On June 14, 1985, both cases were reassigned to this court. The parties have filed cross motions for summary judgment and stipulated to the relevant facts. The United States and a number of foreign governments have filed amicus briefs in support of the foreign-commerce argument made by the plaintiffs. But for the following reasons, the court never reaches the foreign-commerce question.

I.

Motion to Reconsider

While these cases were still before Judge Marshall, the Board filed a motion to dismiss in both actions partly founded upon the argument that the foreign parents lacked standing to challenge the tax assessed on their domestic subsidiaries. In reliance on the Seventh Circuit case *Alcan Aluminum Ltd. v. Department of Revenue of the State of Oregon*, 724 F.2d 1294, 1299 (7th Cir. 1984) ("*Alcan II*"), Judge Marshall rejected the Board's stand-

ing argument in the Alcan case and denied the motion.[2] *Alcan Aluminum Ltd. v. Franchise Tax Bd. of the State of California*, No. 84 C 6932, slip op. at 3 (N.D. Ill. January 10, 1985). In its motion for summary judgment, the Board renews its standing argument and asks this court to reconsider the standing issue.

In *Alcan II*, as in these related cases, the foreign parent corporation sought to restrain state tax officials from applying the unitary apportionment method of taxation to a domestic subsidiary. The key distinguishing feature of *Alcan II*, however, was that in that case the state tax officials had not yet assessed the tax on the domestic subsidiary. Judge Kocoras granted the defendant's motion to dismiss in that case based on his ruling that the foreign parent lacked standing to challenge the state action and that the case was not ripe for decision. *Alcan Aluminum Ltd. v. Department of Revenue of the State of Oregon*, No. 82 C 3388, slip op. at 5-7 (N.D. Ill. March 8, 1983), *aff'd*, 724 F.2d 1294 (7th Cir. 1984). In *Alcan II*, the Seventh Circuit affirmed and agreed with Judge Kocoras that the case was not yet ripe for decision because the tax had not yet been assessed. *Alcan II*, 724 F.2d at 1295 & 1299. In so holding, the Seventh Circuit finished its opinion with the following statement:

> We express *no views* as to whether [Alcan] will have standing to challenge [the Oregon Department of Revenue's] action if [the Department does] assess Alcancorp as part of a unitary business including [Alcan].

Id. at 1299 (emphasis added).

In his opinion rejecting the Board's standing argument, Judge Marshall relied on the following excerpt from *Alcan II*:

> The United States Court of Appeals for the Ninth Circuit, in a case factually similar to the present case, apparently has held that the foreign parent's action is not ripe until a tax has been assessed and the domestic subsidiary has exhausted its state remedies. *Shell Petroleum, N.V. v. Graves*, 709 F.2d 593, 597 (9th Cir. 1983), *cert. denied*, 464 U.S. 1012 (1983). In *Shell*, however, the parent's only alleged injury was as a shareholder of its subsidiary. The parent alleged no apparent injury as a basis for standing. *Id.* at 595. Thus, the subsidiary's state remedy fully protects the parent's interests. The present case is distinguishable. Appellant has alleged an independent injury as a basis for standing. It claims an unconstitutional burden on its foreign commerce. If appellant's allegations as to its standing are accepted as true, its interests and those of Alcancorp are not identical. (citation omitted). Thus, Alcancorp's state remedy does not protect appellant fully. As soon as the tax is assessed against Alcancorp, the threat of injury to appellant will be immediate. Nothing in the Tax Injunction Act requires appellant to wait while Alcancorp pursues its own remedies under Oregon law for its own injury.

[2] The Board withdrew its motion to dismiss in the Imperial case after this ruling.

Alcan II, 724 F.2d at 1299. Judge Marshall understood this portion of the opinion to be an indication that a foreign parent corporation has standing to challenge the imposition of a tax on its subsidiary when the parent alleges that the tax burdens its foreign commerce. *Franchise Tax Bd.*, slip op. at 2. This court cannot agree. The Seventh Circuit did not make a finding that Alcan had standing in *Alcan II*; instead, it held that once the Oregon tax was assessed on Alcan the case would be *ripe* because at that point Alcan would experience the threat of injury. Consequently, unlike in *Shell*, the foreign parent would not have to wait for the domestic subsidiary to exhaust state remedies for the case to become ripe.

While both ripeness and standing are doctrines derived from general notions of justiciability and at times can involve inquiries that are intermingled, the doctrines are by no means identical. Ripeness is a focus on the *timing* of the lawsuit, particularly whether the alleged injury has become mature. *See* 13 C. Wright, A. Miller & E. Cooper, *Federal Practice and Procedure: Civil* ¶ 3531, at 350 (1984). The doctrine of standing is not a focus on the timing of the lawsuit but rather on the *party* who brings the suit. *Id*, § 3531, at 339. In fact courts frequently deny stockholders such as Alcan or Imperial standing to sue even though it is clear that the stockholder has already been injured because the

injury is an indirect result of an injury to the corporation. *See Twohy v. First Nat'l Bank of Chicago*, 758 F.2d 1185, 1194 (7th Cir. 1985); *Club Assistance Program, Inc. v. Zukerman*, 594 F. Supp. 341, 348 n.15 (N.D. Ill. 1984) (Shadur, J.). Stated alternatively, those courts made the finding that the plaintiffs in those suits did not have standing to sue even though those cases were ripe for decision.

Moreover, this court cannot ignore the Seventh Circuit's explicit statement in *Alcan II* that the ruling was based solely on the ripeness question and that it expressed no view on the question of whether Alcan would have standing once tax was assessed. *Alcan II*, 724 F.2d at 1299. Even assuming Alcan and Imperial are correct in their argument that the Seventh Circuit did express its views on the standing issue, such an expression would be obiter dictum in light of the court's ripeness ruling and hence not binding on this court. Therefore regardless of which interpretation of *Alcan II* this court adopts, the court must confront the standing issue directly.

II.

Standing to Sue

Under general principles of corporate law, stockholders of a corporation have no personal or individual right of action against third persons for damages that result indirectly to the stockholders because of an injury to the corporation. *Twohy*, 758 F.2d at 1194. Applying this principle in circumstances virtually identical to those here, courts in three different circuits have found that a foreign parent corporation does not have standing to challenge the tax assessment of that corporation's domestic subsidiary. *EMI Ltd. v. Bennett*, 738 F.2d 994, 996-99 (9th Cir. 1984), *cert. denied*, 469 U.S. 1073 (1984); *Shell Petroleum, N.V.*, 709 F.2d at 595-96; *Alcan II*, slip op. at 5-6 (Kocoras, J.); *Alcan Aluminum Ltd. v. Franchise Tax Bd. of the State of California*, 558 F. Supp. 624, 629 (S.D. N.Y. 1983), *aff'd*, No. 83-7236 (2d Cir. June 17, 1983), *cert. denied*, 104 S.Ct. 1457 (1984). Moreover, in his concurrence in *Simon v. Eastern Kentucky Welfare Rights Org.*, 426 U.S. 26 (1976), Justice Stewart stated the following:

> I add only that I cannot now imagine a case, at least outside the First Amendment area, where a person whose tax liability was not affected ever could have standing to litigate the federal tax liability of someone else.

Simon v. Eastern Kentucky Welfare Rights Org., 426 U.S. 26, 46 (1976) (Stewart, J., concurring). Justice Stewart's statement is equally applicable to state tax liability.

Because the foregoing cases adequately state the grounds for the finding that Alcan and Imperial have no standing, this court will not belabor the point here. Suffice it to say that the domestic subsidiaries can raise the foreign-commerce claim in suits which they bring and that authority exists for the proposition that the United States itself can bring suit to challenge the burden on foreign commerce. *See United States v. Solomon*, 563 F.2d 1121, 1126-29 (4th Cir. 1977) (cases cited therein). Furthermore, the demands for information which both Alcan and Imperial complain of were made to the domestic subsidiaries, not to Alcan or Imperial. Even if those demands constituted a basis for standing, it would be for the limited purpose of attacking the demands themselves rather than the tax liability of those domestic subsidiaries. *See EMI Ltd. v. Bennett*, 560 F. Supp. 134, 136 (N.D. Cal. 1982), *aff'd*, 738 F.2d 994 (9th Cir. 1984), *cert. denied*, 469 U.S. 1073 (1984).

Conclusion

The court grants the Board's motion for summary judgment in both the Alcan and the Imperial cases. Both cases are dismissed.

ENTER:

/s/ Ann Claire Williams

Dated: JUL 29 1987

Appendix C

(Filed June 17, 1983)

83-7236

UNITED STATES COURT OF APPEALS

For the Second Circuit

At a stated Term of the United States Court of Appeals the Second Circuit, held at the United States Courthouse, City of New York, on the 17th day of June One Thousand Nine Hundred and Eighty-three.

PRESENT:

Hon. Ellsworth A. Van Graafeiland,

Hon. Lawrence W. Pierce

Hon. John Minor Wisdom,*

Circuit Judges

ALCAN ALUMINUM [SIC] LIMITED,
Plaintiff-Appellant,

THE FRANCHISE TAX BOARD OF THE STATE OF CALIFORNIA, operating through its New York Office; FRANK GOODMAN, individually and as District Manager, New York Office of the Franchise Tax Board of the State of California; and JOSEPH E. GEORGHEGAN [sic], Individually and as Supervisor—Audit Group, New York Office of the Franchise Tax Board of the State of California,

Defendants-Appellees.

* Senior Circuit Judge of the Fifth Circuit, sitting by designation.

N.B. Since this statement does not constitute a formal opinion of this court and is not uniformly available to all parties, it shall not be reported, cited or otherwise used in unrelated cases before this or any other court.

ORDER

Alcan Aluminum [sic] Limited appeals from a judgment of the United States District Court for the Southern District of New York (Goettel, J.) dismissing its complaint against the Franchise Tax Board of the State of California and two of its New York office employees. We find appellant's contentions without merit and affirm substantially for the reasons stated in the opinion of the district court reported at 558 F. Supp. 624.

/s/ E. A. Van Graafeiland
/s/ L. W. Pierce
/s/ John Minor Wisdom